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Fitch: Federal Action Needed to Prevent Delays on Transportation Projects

Fitch Ratings-New York/San Francisco-23 September 2020: Transportation projects that rely on federal funding are at risk of being delayed or cancelled unless Congress reauthorizes federal spending from the Highway Trust Fund (HTF) and provides resources to support the fund, Fitch Ratings says. HTF funding uncertainty discourages investment in substantial, multi-year infrastructure projects as these require long-term planning and funding commitments. The HTF and state transportation budgets depend on federal fuel tax revenues, which were declining even before the coronavirus pandemic due to improved fuel efficiency and the static fuel tax, which has not changed since 1993. HTF spending exceeded fuel tax revenues by about 26% in 2019.

Gas consumption and gas tax revenues declined dramatically at the height of the pandemic, resulting in a meaningful reduction in HTF funds. While gas sales rebounded in June from their historical low in April 2020, consumption is still below typical summer levels according to the US Energy Information Administration (EIA). Factors including a reduction in travel and commuting due to high unemployment and the increase in remote working are expected to keep motor gasoline consumption below 2019 levels through 2021 according to the EIA's September 2020 Short- Term Energy Outlook, further pressuring fuel tax revenues. Many states increased fuel taxes and toll revenues in recent years to help fill transportation infrastructure revenue gaps but these taxes may not be sufficient considering federal funding comprises approximately a quarter of spending on highways.

The Fixing America's Surface Transportation (FAST) Act, which will expire on Sept. 30, 2020, allocates billions of dollars from the HTF to state governments, and the Act also provides for federal general fund transfers to the HTF. Federal transportation allocations to the states will halt, and the HTF could become insolvent as soon as federal FY 2022 unless Congress takes action. Based on the history of HTF reauthorizations, Fitch expects Congress will eventually reauthorize the program and maintain HTF solvency.

The HTF historically received uninterrupted funding even during past short-term authorization lapses, although it relied on federal general fund transfers to remain solvent. The March 2020 Congressional Budget Office (CBO) baseline projections indicate the HTF highway subaccount would run out of money in FY 2022 absent additional subsidies or a structural shift in the fund. Fitch notes the CBO projections are based on pre-pandemic budget and economic projections so insolvency could actually occur sooner absent Congressional action.

Raising federal fuel taxes going forward under the program to cover shortfalls or broader reform of HTF revenues and spending will be difficult in light of the weak economic environment, a ballooning federal deficit the CBO projects will be $3.3 trillion in 2020, and pressing infrastructure demands. Given increased vehicle fuel efficiency, alternative taxes have received more attention. Registration fees and taxes on fuel efficient or electric vehicles, while more feasible, would generate a relatively small amount of revenue compared to HTF spending. Other taxing options that could support the HTF, such as a tax on vehicle miles travelled or a highway freight tax, may be difficult to implement because of the costs of implementing and enforcing a new tax system. An additional tax burden would also be unpopular during the nascent economic recovery.

Congress has not arrived at a consensus on bills proposed earlier this year that would extend the FAST Act, and these bills do not include a long-term structural solution for the HTF. Fitch recognizes there are competing policy and funding priorities placed on the federal government as a result of the coronavirus pandemic. This potentially makes funding decisions regarding the HTF more difficult. Congress may choose to reduce federal highway spending or postpone a longer-term commitment to stabilizing HTF funding.

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